

Internal Revenue Service
memorandum

TR 45-2124-91

BR2:DRFuller

date:

to: Case Manager ([REDACTED] District) [REDACTED]
Group Manager ([REDACTED] District) [REDACTED]

from: Acting Associate Chief Counsel (Employee Benefits
and Exempt Organizations) CC:EE

subject: [REDACTED] --Clarification of Technical Advice Memorandum

You have requested our assistance to determine whether the Examination Division of the [REDACTED] District ("Examination Division") correctly followed the guidelines enumerated in the technical advice memorandum issued on December 13, 1990. That technical advice memorandum analyzed whether any portion of the hourly expense allowance paid to the flight crews of [REDACTED] (" [REDACTED] ") was excludable from "wages" within the meaning of section 3401(a) and 3121(a) of the Internal Revenue Code. This clarification has been requested because the [REDACTED] Appeals Office ("Appeals Office") has returned the employment tax case to the Examination Division for further action. The Appeals Office's primary rationale for returning the case is that the Examination Division did not follow the guidelines set forth by the National Office in the technical advice memorandum.

After carefully reviewing this matter, we reiterate our prior conclusion that the [REDACTED] District is in the best position to analyze the facts and circumstances of this case. Consequently, we believe the case was generally developed in accordance with our technical advice memorandum. However, the Examination Division should reevaluate the application of Rev. Rul. 84-164, 1984-2 C.C. 63, to this case.

FACTS

[REDACTED] has undergone a federal employment tax audit for the years [REDACTED] through [REDACTED]. During the years at issue, [REDACTED] paid its flight crews an hourly travel allowance in addition to normal wages on both overnight and nonovernight flights. The primary audit issues are the extent to which these hourly payments constitute "wages" for income tax and FICA tax purposes. On December 13, 1990, this office issued a technical advice memorandum concerning those issues. The Examination Division issued a Notice of Proposed Adjustment on February 15, 1991. That notice holds [REDACTED] liable for income tax and FICA tax

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withholding on the full amount of the travel allowances.

█████'s case was transferred to the Appeals Office in September 1991. The Appeals Office briefly examined the files associated with the case and determined that the Examination Division had not followed the National Office's guidelines. Consequently, the Appeals Office returned the case to the █████ District in October 1991 for reconsideration. On November 15, 1991, you requested clarification of the technical advice memorandum. In a telephone conference on December 17, 1991, the technical assistance request was modified and the National Office was asked to examine whether the Examination Division's determination was consistent with the technical advice memorandum.

DISCUSSION

The transmittal memorandum from the Appeals Office cites several reasons for returning the case to the Examination Division. The central theme of the transmittal memorandum is that the Examination Division failed to follow numerous directives from the National Office. However, the only memorandum that is pertinent to this case is the technical advice memorandum issued to the █████ District since it dealt with the specific taxpayer, facts, and issues in question. Consequently, only the technical advice memorandum needs to be examined to determine whether the █████ District's determination is consistent with the National Office's guidance.

The technical advice memorandum's primary focus was whether any portion of the hourly expense allowance paid to █████'s flight crews was excludable from wages within the meaning of sections 3401(a) and 3121(a) of the Code. To be excludable, it must be reasonable to believe that the employee will be able to exclude the benefit from income under section 132 at the time the benefit is provided. As you know, █████ maintains that the hourly payments were reimbursements for the flight crews' travel expenses rather than additional compensation to its employees. █████ further maintains that it had a reasonable belief for anticipating that those amounts were spent by the employees for meals and other incidental business travel expenses.

In our memorandum, we stated that whether it is reasonable for the employer to believe that an employee will be able to exclude any or all of such benefit from gross income under section 132 of the Code necessarily depends on the facts and circumstances of each particular case. This determination entails an examination of whether █████ had a reasonable belief that the expenses would be substantiated under section 274 either through actual or deemed substantiation. The amount of taxable wages is equal to the amount in excess of what it was reasonable

for the Taxpayer to believe was excludable. As a starting point and solely for the purpose of assessing the reasonableness of [REDACTED]'s belief, we suggested using the Federal M&IE rate for the locality in which the expenses were incurred.

We specifically avoided undertaking a factual analysis in the technical advice memorandum since the District Office is in the best position to reconcile any conflicting factual allegations and to make a final determination as to what [REDACTED] actually believed or could have believed was reasonable at the time the payments were made. In making this determination, we advised you to take into consideration all of the relevant facts and circumstances. If [REDACTED] had knowledge that its employees were not substantiating these amounts, then the reasonableness of its belief is questionable.

In support of your decision to include the full amount, you recently provided us with a list of 14 factors which were examined when determining the reasonableness of [REDACTED]'s belief. We specifically avoid analyzing each specific factor and only note that it was reasonable to consider those factors as a whole. Furthermore, we do not opine on the weight that should be accorded to any one factor. Instead, we reiterate our prior position that the District Office is in the best position to reconcile any conflicting factual allegations and to make a final determination on whether it was reasonable to believe that an employee would be able to exclude the benefits from income under section 132 of the Code.

It is our understanding that you exhaustively developed this case and did so to a greater extent than any comparable case within the airline industry. This exhaustive analysis and daily exposure to the issue presented places the [REDACTED] District in a unique position to analyze and weigh each relevant fact. Consequently, with only one exception, we can not say that the case was developed contrary to the guidelines mentioned in the technical advice memorandum. We reiterate that we are not in a position to substitute our judgment for yours.

As noted, only one aspect of the case appears to need further clarification--the application of Rev. Rul. 84-164, 1984-2 C.B. 63. Rev. Rul. 84-164 holds that per diem allowances for business travel away from home (for periods of less than 30 days) in the amount of \$14 per day are deemed substantiated under § 1.274-5(c). In the memorandum, we noted that [REDACTED] could rely on that ruling to deem the substantiation of \$[REDACTED] per day. For amounts in excess of \$[REDACTED], it must have been reasonable for [REDACTED] to believe that its employees would actually substantiate their expenses pursuant to section 274(d) of the Code. Of course, the ruling does not relieve the taxpayer of the responsibility of substantiating the time, place, and business purpose of the travel. Furthermore, the boarded meals may be considered as a

factor which might possibly reduce this rate of deemed substantiation.

We trust that this memorandum has helped clarify the application of the technical advice memorandum. If you have any other questions or comments, please do not hesitate to contact us.

JAMES J. McGOVERN
Acting Associate Chief Counsel

By: _____

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